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February 16, 1993

Federal Communications Commission
Office of the Secretary
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

Re: MM Docket No. 92-265

Dear Sir/Madam:

Enclosed for filing please find the original and nine copies of the reply comments of Discovery Communications, Inc. in the above-captioned matter.

Sincerely,

Jerianne Timmerman
Jerianne Timmerman

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992 Development of Competition and Diversity in Video Programming Distribution and Carriage	MM Docket No. 92-265

REPLY COMMENTS OF DISCOVERY COMMUNICATIONS, INC.

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In the Matter of Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992 Development of Competition and Diversity in Video Programming Distribution and Carriage	MM Docket No. 92-265

REPLY COMMENTS OF DISCOVERY COMMUNICATIONS, INC.

Discovery Communications, Inc. ("Discovery") hereby replies to the comments filed with respect to the Commission's Notice of Proposed Rulemaking to implement sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992 ("Cable Act"). These reply comments specifically address (i) the definition of attributable interest; (ii) the showing of harm required to establish a violation of section 19; (iii) the meaning of discrimination under section 19; and (iv) the scope of the exclusive-dealing prohibition.

I. SUMMARY

In drafting these regulations, the Commission should not interpret the terms of the Cable Act literally, but should exercise its inherent discretion to promulgate feasible and practical regulations that do not unnecessarily impinge on the marketplace and that do not have the unintended Effect of harming consumers.

Consistent with this basic principle, "attributable interest" should be defined as "control," as only a cable operator that actually controls a programmer could force it to engage in conduct against its own interests. Similarly, the Commission should interpret section 19 as requiring a showing of potential harm to competition and as prohibiting only those price differences and those exclusive contracts that could injure competition. The Commission also should expressly allow volume discounts, price differentials for different types of delivery systems, and other price differences which do not harm competition.

II. THE COMMISSION IS ENTITLED TO EXERCISE BROAD DISCRETION.

Some commenters reprimanded the Commission for considering regulations which do not take the exact steps that the commenters believed Congress to have mandated in the Cable Act. Those commenters ignore the broad discretion and flexibility that administrative agencies possess in promulgating regulations. The Commission may obviously consider "feasibility and practicality" in promulgating these regulations. Permian Basin Area Rate Cases, 390 U.S. 747, 777 (1968). It may take an administrative approach not explicitly provided for in the Cable Act on grounds of administrative necessity. See Alabama Power Co. v. Costle, 636 F.2d 323, 358 (D.C. Cir. 1979). Moreover, the Commission need not apply the literal terms of the Cable Act if doing so would mandate fruitless expenditures of effort, and it may properly overlook circumstances that in context may be considered de minimus.[1] Id. at 360. Thus, as a general matter the Commission should not rigidly interpret the terms of the Cable Act, but should consider the competitive conditions of the cable television industry to promulgate regulations that are practical, feasible and respectful of marketplace realities.

III. "ATTRIBUTABLE INTEREST" SHOULD BE DEFINED AS CONTROL.

The Notice asked for comments on the definition of "attributable interest" for the purpose of determining whether a cable programmer is vertically integrated with a cable operator. In its comments (at pages 16-17), Discovery urged the Commission to define "attributable interest" as "control" (holding 50% or more of the programmer's outstanding voting securities or having the contractual power to designate 50% or more of the programmer's directors). Because a programmer that favored a cable-operator investor by restricting sales to other distributors would suffer the negative consequences of sales and revenue losses, a cable operator would have to control the programmer in order to force it to incur such losses.[2]

1/ For example, price differentials de minimus in amount or not sustained over time may be presumed to be outside the regulatory scope of section 19 of the Cable Act because such de minimus price differences cannot injure competition.

2/ In its comments (at pages 11-12), Discovery explained that, to succeed in the marketplace, programmers must provide fair terms. Discovery does not -- indeed, cannot -- give preferential treatment to its cable operator owners because to do so would deter other cable system customers from carrying its services, thereby reducing its subscriber base and, consequently, its subscriber fees and advertising revenues.

A number of commenters agreed with Discovery that control is the proper standard, but some proposed tests for control which are too complex. See, e.g., Comments of Group W Satellite Communications at pages 2-8 (suggesting two-fold analysis with broadcast attribution rules as threshold and additional analysis focusing on opportunity of particular entities to engage in anti-competitive behavior as second step). Discovery urges the Commission to adopt a simple, bright-line "control" test such as it proposed. Unlike more complex tests, Discovery's standard can be easily administered in practice and places a minimal regulatory burden on the Commission.3/

Those commenters advocating a standard below that of "control" failed to present evidence or even arguments showing how a cable operator holding a minority interest in a programmer could coerce that programmer to act against the programmer's own best interests by refusing to deal with or discriminating against actual or potential distributor-customers.4/ While a cable

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3/ Other commenters have agreed with Discovery's position. See, e.g., Comments of United Video, Inc. at pages 12-13; Liberty Media Corporation at pages 11-18; The National Cable Television Association, Inc. at pages 14-19.

4/ See, e.g., Comments of Coalition of Small System Operators at pages 2-4 (advocating 20% ownership standard without explaining why such standard is necessary to fulfill pro-competitive purposes of section 19); Nynex Telephone Company at pages 7-8 (arguing against "control" standard by merely stating that an entity does not have to control a programmer to exert influence); CableAmerica Corporation at pages 12-13 (urging 5% ownership threshold without explaining how such minimal ownership would cause programmers to give preferential treatment to related distributors); The Wireless Cable Association

Continued

operator with a non-controlling interest may be represented on a programmer's board and can make its voice heard, it does not have sufficient power to compel a programmer to forgo profitable business. Illustratively, despite considerable cable-operator investment in Discovery, Discovery has always made its own independent decisions as to whom to sell programming and at what price. As mentioned in its comments, the Discovery Channel and The Learning Channel both do significant business with alternative technology distributors.

IV. SECTION 19 REQUIRES SHOWING OF POTENTIAL HARM TO COMPETITION.

Discovery agrees with those comments emphasizing that Section 19 is intended to ensure that consumers have access to programming, not to promote business interests of individual multichannel competitors. Thus, the Commission should not promulgate regulations allowing a multichannel distributor to file a complaint against a vertically integrated programmer on the grounds that the programmer significantly hindered the distributor from delivering that programmer's programming to subscribers. Rather, the unfair or deceptive practice complained of must have sufficiently hindered the distributor's delivery of comparable programming so that the distributor's ability to compete in the marketplace for the distribution of programming is substantially impaired. See Comments of Time Warner

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International, Inc. at pages 22-28 (advocating 1% ownership standard without showing how a 2% or other small minority owner could unduly influence a programmer in practice).

Entertainment Company at pages 4-11; The National Cable Television Association at pages 6-10; Group W Satellite Communications at pages 8-9; United Video, Inc. at pages 15-19; Rainbow Programming Holdings, Inc. at pages 4-6.

To ensure that the focus of these regulations remains on the consumers, Discovery also urges the Commission to consider the suggestion of International Family Entertainment, Inc. ("IFE") to require that a company challenging a programmer's alleged discrimination agree to pass through to its customers any lower rate it obtains from the vertically integrated programmer as a result of the proceeding. Comments of IFE at pages 7-8. By requiring such a pass-through of lower rates to subscribers, the Commission would ensure that the Cable Act benefits its intended beneficiaries -- the consumers. Similarly, the Commission should only prohibit price differences which are of sufficient magnitude to affect consumer prices.

The commenters arguing that section 19 does not require any showing of potential competitive harm appear to misread the statutory language.[5/] Section 19(b) of the Cable Act (section 628(b) of the Communications Act) clearly prohibits unfair or deceptive "acts or practices, the purpose or effect of which is

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5/ See, e.g., Comments of Coalition of Small System Operators at pages 6-7 (asserts that showing of "actual harm" is not required but makes no reference to the "hinder significantly" statutory language); U.S. West Communications, Inc. at pages 11-12 (flatly states that discrimination is a *per se* violation of Cable Act, but fails to explain why a showing of significant hindrance is not required, given the statutory language).

to hinder significantly or to prevent any multichannel video programming distributor from providing . . . programming to subscribers or consumers."

Moreover, some commenters have engaged in a tortured structural analysis in an attempt to argue that the conduct specified in Section 628(c) is *per se* prohibited, even if it does not hurt competitors or consumers. *See*, *e.g.*, Comments of DirecTv at pages 9-12; CableAmerica Corporation at pages 13-15. But they ignore Section 628(c)(1) requiring the Commission to promulgate regulations "to specify particular conduct that is prohibited by subsection (b)," which prohibits only unfair or deceptive acts or practices that significantly hinder competition. Thus, the particular conduct delineated in section 628(c) is prohibited only if such conduct significantly hinders competition, as clearly required in section 628(b). *See* Comments of The National Cable Television Association, Inc. at pages 6-9; EMI Communications Corporation at pages 8-9; Tele-Communications, Inc. at pages 5-7.

V. SECTION 19 DOES NOT PROHIBIT ALL PRICE DIFFERENCES, BUT ONLY DISCRIMINATORY PRICE DIFFERENCES.

As Discovery noted in its comments (at pages 20-23), the Cable Act does not prohibit all price differences by vertically integrated programmers. Indeed, Discovery emphasized that section 19 expressly permits price differences (i) based on economic benefits attributable to the number of subscribers served by distributors, or (ii) justified by cost differences. Thus, Discovery urged the Commission to expressly allow various types of discounts, such as volume, group-buying, and introductory and promotional. Discovery also urged the Commission to permit price differentials for different types of delivery systems when justified by different costs or benefits to the programmer.

Numerous commenters agreed with Discovery's discussion of discrimination.[6/] Commenters noted that price differentials can in fact further the intent of the Cable Act by increasing programming available to the public.[7/]

If the Commission forced programmers to provide programming to all distributors at uniform prices (regardless of the costs incurred or benefits received by the programmer in serving various types of distributors), the revenues of the programmers would suffer, thereby decreasing the ability of programmers to produce new and original programming for consumers. See Comments of International Family Entertainment, Inc. at page 9; EMI Communications Corporation at pages 9-11. Thus, the imposition of blanket prohibitions on price differences or the establishment

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6/ See, e.g., Comments of EMI Communications Corporation at pages 3-8; Turner Broadcasting System, Inc. at pages 8-14; E! Entertainment Television, Inc. at pages 8-10; Time Warner Entertainment Company at pages 23-27; Superstar Connection at pages 47-52; Affiliated Regional Communications, Ltd. at pages 14-15; Liberty Media Corporation at pages 21-44.

7/ The Commission itself has recognized that price differentials can in fact encourage program diversity. Notice at ¶ 15 (seeking comment on situations in which uniform pricing requirements could reduce amount of programming available to subscribers).

of uniform pricing structures (as urged by some commenters) would be counter-productive to the stated Congressional goal of increasing the programming available to consumers.[8/]

A. The Commission Should Allow Volume and Other Similar Discounts.

With regard to the specific types of price differentials discussed by Discovery, the comments showed particularly strong support for allowing programmers to provide volume and other discounts, such as prepayment discounts and performance discounts.[9/] The commenters noted that volume discounts exist for nearly all products and services sold in the United States and are particularly important for services such as cable program networks, which need to increase their subscriber base to capture advertising revenue and subscriber fees.[10/]

8/ *See*, *e.g.*, Comments of Advanced Communications Corporation at page 6; The Attorneys General of Texas, Maryland, Ohio, and Pennsylvania at page 10. These comments urging the Commission to require uniform pricing ignore both the Congressional policy expressed in the Cable Act (§ 2(b)(2)) to rely on the marketplace *and* the reality of the cable television market itself (*i.e.*, that programmers bear differing costs and receive differing benefits in serving various distributors).

9/ *See*, *e.g.*, Comments of United Video, Inc. at pages 25-27; Time Warner Entertainment Company at page 27; Landmark Communications, Inc. at pages 18-20; Coalition of Small System Operators at page 5; E! Entertainment Television, Inc. at pages 9-10; Turner Broadcasting System, Inc. at pages 12-14; Liberty Media Corporation at pages 38-39; Tele-Communications, Inc. at pages 18-23.

10/ In its comments (at pages 10-11), Discovery described how advertising revenues, which depend upon the size of a program service's subscriber base, are crucial to a programmer's success. Discovery has employed both volume discounts (*e.g.*, increasing charges to affiliates if

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Volume and other similar discounts produce economic benefits for programmers (by increasing their subscriber base and revenues), distributors (who receive lower prices from programmers), and subscribers (who receive lower prices from distributors and enjoy new programming produced by programmers with their enhanced revenues). Accordingly, the Commission in its regulations should permit programmers to offer such discounts.

B. The Commission Should Permit Price Differentials Between Types of Delivery Systems.

Commenters also agreed with Discovery's position that programmers should be permitted to charge different prices to different types of delivery systems.11/ Indeed, in certain cases, as for example the sale of programming to the home satellite dish ("HSD") market, price differentials are so clearly justified by the differing costs incurred and benefits received by programmers in providing program services to different types of distributors that they should be presumed to be non-discriminatory.

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certain system penetration levels were not achieved) and introductory offers (*e.g.*, not charging subscribers in newly launched cable systems for an initial period) to build its audience for The Discovery Channel and The Learning Channel.

11/ *See*, *e.g.*, Comments of Turner Broadcasting System, Inc. at 8-12; Affiliated Regional Communications, Ltd. at pages 4-8; EMI Communications Corporation at pages 4-8; Liberty Media Corporation at pages 26-37.

Programming vendors incur additional administrative and maintenance costs to serve the HSD market, including anti-piracy and tier bit costs.[12/] Programming vendors also receive greater benefits from providing programs to cable operators than to HSD distributors. For example, cable operators invest in plant and equipment to create and maintain delivery systems that benefit subscribers and, ultimately, programming vendors. In contrast, HSD distributors often act as little more than sales agents or middlemen; they do not build physical plants to push penetration rates, help increase the audience that generates programmers' advertising revenues, or commit resources to market program networks as cable systems do.[13/] For these reasons, programmers including Discovery argue that the Commission should not force them to sell their programming services to HSD distributors at the same price they sell to cable operators. See Comments of EMI Communications Corporation at pages 4-8; Turner Broadcasting System, Inc. at pages 8-12; Time Warner Entertainment Company at pages 25-27.

12/ The Commission has recognized that the delivery of signals to individual HSD subscribers may be more expensive and less secure from piracy than delivery to the head end of a cable system. Notice ¶ 17.

13/ Turner Broadcasting's comments emphasized the importance of mass penetration (which determines advertising revenues) to cable programmers. Cable operators (because of their nationwide penetration) have provided Turner Broadcasting, and other programmers such as Discovery, with the subscriber and advertising base to support programming costs. Satellite dish distributors have not provided such a subscriber base and are therefore not as critical to programmers.

Discovery prices its programming to distributors based on the economics of the marketplace, and the Commission's regulations should allow it to continue doing so. As stated in its comments (at page 12), Discovery offers the same rate cards to cable operators, SMATV, and MMDS systems that initially licensed The Discovery Channel at the same time. Although Discovery charges higher rates to TVROs, these higher rates incorporate additional investment in scrambling equipment and in the tier bit data stream that "authorizes" TVRO household reception. Because TVRO distributors serve rural, un-wired regions, they generally have fewer subscribers than other distribution systems. As a result, they are more costly to serve and produce fewer benefits to Discovery in terms of either subscriber fees or advertising revenues.

C. Other Discrimination Issues.

With regard to other price differential issues raised in the comments, Discovery disagrees with those commenters who have urged the Commission to establish zones of presumptively reasonable price differentials.[14/] The boundaries of such zones would be extremely difficult to determine, given the numerous differences among services, costs, carriage arrangements, technologies and competitive conditions.[15/] Discovery agrees

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14/ *See*, *e.g.*, Comments of The National Cable Television Association, Inc. at pages 21-23; Viacom International Inc. at pages 18-20; Time Warner Entertainment Company at pages 28-30; Tele-Communications, Inc. at pages 13-14.

15/ One suggestion that the Commission establish three zones to Continued with other commenters that such an approach poses a real danger of arbitrariness and capriciousness and of inhibiting price competition among programmers. _See_ Comments of Liberty Media Corporation at pages 45-17.

Also, the Commission should reject the contention of The Wireless Cable Association that a distributor aggrieved by programmer violations of section 19 has a cause of action, even if it does not directly compete against a cable operator with an attributable interest in the programmer. _See_ Comments of The Wireless Cable Association International, Inc. at pages 30-34. Rather, standing to bring a section 19 claim against a programmer should be limited solely to a distributor competing with a cable operator with an attributable interest in the programmer in the geographic market in which the distributor unsuccessfully sought programming. Anticompetitive harm can occur only if two distributors competing in the same market receive discriminatorily disparate treatment from a programmer because one of the distributors is affiliated with the programmer. It is irrelevant for the purposes of section 19 that a vertically integrated programmer treats distributors differently when the distributors are not competing against each other. _See_ Comments of E! Entertainment Television, Inc. at page 6.

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evaluate price differentials (irrebuttably reasonable, rebuttably reasonable and rebuttably unreasonable) appears particularly unwieldy. _See_ Comments of Time Warner Entertainment Company at pages 28-30.

VI. THE COMMISSION SHOULD PERMIT EXCLUSIVE DEALING CONTRACTS WHICH DO NOT HARM COMPETITION.

In its comments (at pages 26-30), Discovery noted that exclusive dealing has many procompetitive benefits. The Commission should therefore allow exclusive-dealing arragements unless they prevent competing multichannel video program distributors from obtaining programming sufficient for such distributors to survive in the market.16/ Numerous commenters have supported Discovery's position. See, e.g., Comments of Cablevision Industries Corporation at pages 15-19; Turner Broadcasting System, Inc. at pages 5-8; Tele-Communications, Inc. at pages 23-30; Liberty Media Corporation at pages 47-50; Affiliated Regional Communications, Ltd. at pages 15-18.

Those commenters that have called for a rigid ban on exclusive programming arrangements17/ have failed to refute that procompetitive benefits result from exclusive dealing, as the Commission itself has noted. See 3 FCC Rcd 5299, 5309-10 (1988). Commenters attacking exclusive dealing appear to approach the practice from the viewpoint of an individual distributor aggrieved by its inability to obtain a particular program service. However, as pointed out above, exclusive

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16/ As discussed previously, neither competition nor consumers are injured even if a multichannel video program distributor cannot obtain a particular program due to the existence of an exclusive dealing arrangement, assuming such distributor can obtain substitute programming.

17/ See, e.g., Comments of Liberty Cable Company, Inc. at pages 14-18; DirecTV, Inc. at pages 26-29; Bellsouth Telecommunications, Inc. at pages 7-10.

contracts are anti-competitive and should be prohibited only when they deprive an alternative distributor of the programming necessary for it to remain in the market as a distributor. Due to their generally procompetitive effects, the Commission should prohibit only the narrow range of exclusive contracts that have deprived alternative distributors of programming vital to their commercial survival.

Respectfully submitted,

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